

4

Posting and Preparing Financial Statements

General Ledger	66
Posting	67
Preparing the Trial Balance	71
Preparing Financial Statements	73
Evaluating the Financial Statements	78
Chapter Summary	79
Key Terms	79
Further Reading	79
Put It into Practice	80
Review Questions	81
Practice Exercises	82
Appendix 4.1	95

LEARNING
OUTCOMES

After reading this chapter, you should be able to:

- post transactions from the general journal to the general ledger
- prepare a trial balance
- prepare financial statements

In Chapter 2, we recorded the **opening balance** in a **general journal**, and in Chapter 3 we recorded transactions for the month of October in the general journal. The next step in the **accounting cycle** is to post these entries to a general ledger.

General Ledger

The **general ledger** provides a summary of the information contained in the general journal. The information from the general journal is summarized by posting or copying the information to the accounts in the general ledger. Without a summary, the firm cannot know what its bank balance is or how much money has been spent to date on any particular account. The summary is also required for preparation of financial statements.

The general ledger contains a sheet for each of the accounts listed on the company's **chart of accounts**, along with the number of the account. The example in Figure 4.1 shows the format for a simple general ledger account. The name of the account is General Bank Account; the number of the account is 100. The **post reference (PR)** is the numerical identifier for each account referenced on the chart of accounts. This makes it easy to cross-reference and identify journal entries.

The columns in the ledger sheet include a column for the year and date, an explanation, the post reference, a column for debit, a column for credit, and a column for the balance. You will notice that the column immediately before the balance is headed "Dr./Cr." This column is used to indicate whether the running balance is a debit balance or a credit balance. It does not refer to the entry made on that line. You will need to calculate the running balance after making each entry in the general ledger accounts.

A general bank account is an asset and usually has a "Dr." balance, unless the account is overdrawn (or "in the red"). If the balance in the bank is negative, you will indicate "Cr." in the column before the balance. The ledger accounts are kept by category in the same order as they appear in the chart of accounts: assets, liabilities, owner's equity, income, and expenses.

General Bank Account					Account No. 100	
Date 20**	Explanation	PR	Debit	Credit	Dr./Cr.	Balance

FIGURE 4.1 Sample general ledger account

Posting

The entries from the general journal must be copied to the individual general ledger accounts. Each debit and credit entry must be posted in the same order as it appears in the general journal. Posting is done as you transfer the debits and credits for each transaction from the general journal to the general ledger.

EXAMPLE

Justin Case, General Journal					GJ1
Date 20**		Description	PR	Debit	Credit
Oct.	1	Opening Entries			
		General Bank Account	6100	1,000	
		Justin Case, Capital	6300		1,000
		<i>To record funds invested by owner</i>			

FIGURE 4.2 Posting entry from the general journal

To post the general journal entry dated October 1 (Figure 4.2) to the general ledger, you would take the following steps (the numbered steps are shown in superscript in the previous and following posting entries):

STEP 1

In the general ledger, find the account called General Bank Account (Figure 4.3). Enter the amount of \$1,000 in the debit column. Because the \$1,000 is debited in the general journal, it must be shown as a debit in the general ledger.

STEP 2

Enter GJ1 in the post reference column of the ledger. This tells anyone looking at the books that the debit came from page 1 of the general journal.

STEP 3

Enter the transaction date in the date column of the ledger as shown in the general journal.

STEP 4

Calculate the running balance.

STEP 5

Indicate whether the balance is a debit or a credit balance in the Dr./Cr. column.

STEP 6

Put the number of the account to which the entry was posted in the post reference box of the general journal (Figure 4.2). Post referencing indicates which transactions have or have not been posted from the general journal to the general ledger, and also indicates the account to which the entry has been posted.

Repeat steps 1 to 6 to post the second line of the general journal entry (the credit side) to the Justin Case, Capital account in the general ledger (Figure 4.3).

The process provides a trail to show the ledger account to which an entry in the general journal was posted, and also shows where the number in the ledger came from. You would continue this process, entering each transaction in the correct general ledger and totalling the amounts in the general ledger to summarize the transactions.

Note that no explanation is required when completing the entry in the general ledger. This is because you have the explanation in the general journal. If you need to know what the \$1,000 posted on October 1 was for, you can refer back to page 1 of the general journal, where the explanation is found. However, an explanation may be added if the bookkeeper wishes to provide extra details regarding an entry.

Once all the journal entries from pages GJ1 and GJ2 have been posted, the general journal for Justin Case's firm will appear as in Figure 4.4.

General Ledgers — Justin Case							
General Bank Account						Account No. 6100	
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
³ Oct.	1		² GJ1	11,000		⁵ Dr.	⁴ 1,000

Justin Case, Capital						Account No. 6300	
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
³ Oct.	1		² GJ1		11,000	⁵ Cr.	⁴ 1,000

FIGURE 4.3 Posting to the general ledgers: General Bank Account and Justin Case, Capital account

Justin Case, General Journal					GJ1
Date 20**		Description	PR	Debit	Credit
Oct.	1	Opening Entries			
		General Bank Account	100	1,000	
		Justin Case, Capital	300		1,000
		<i>To record funds invested by owner</i>			
	1	General Bank Account	100	4,000	
		Personal Loan	205		4,000
		<i>To record loan from father, James Case</i>			
	1	Computer Equipment, Hardware	155	900	
		Justin Case, Capital	300		900
		<i>To record computer equipment invested by owner at fair market value</i>			
	1	Office Furniture and Equipment	158	150	
		Justin Case, Capital	300		150
		<i>To record office furniture invested by owner at fair market value</i>			
		Totals		<u>6,050</u>	<u>6,050</u>

Justin Case, General Journal					GJ1
Date 20**		Description	PR	Debit	Credit
Oct.	5	Telephone Expense	565	300	
		General Bank Account (Cash)	100		300
		<i>To record telephone expense for Oct.</i>			
	5	Office Furniture and Equipment	158	2,000	
		General Bank Account (Cash)	100		500
		Credit Card Debt	210		1,500
		<i>To record furniture purchased from IKEA</i>			
	8	General Bank Account	100	500	
		Justin Case, Capital	300		500
		<i>To record investment of scholarship</i>			
	10	Office Supplies/General Expense	535	580	
		Accounts Payable/General Liabilities	200		580
		<i>To record purchase from Legal Supplies Inc.</i>			
	15	Office Furniture and Equipment	158	100	
		General Bank Account	100		100
		<i>Purchased filing cabinet from Office Equipment Inc.</i>			
	20	General Bank Account	100	3,000	
		Fees Earned	400		3,000
		<i>To record fees billed to Sabourin and paid</i>			
	30	Rent Expense	538	500	
		General Bank Account	100	_____	<u>500</u>
		<i>To record rent paid for one month</i>			
		Totals		<u>6,980</u>	<u>6,980</u>

FIGURE 4.4 All general journal entries posted for October

After Justin Case has posted all the entries made to date on pages GJ1 and GJ2, the general ledger will have the balances shown in Figure 4.5. Note that the

accounts that do not have any entries are omitted at this time. The general ledger accounts will be added as required as we complete the posting.

General Ledgers — Justin Case

General Bank Account						Account No. 100	
<i>Date</i> 20**		<i>Explanation</i>	<i>PR</i>	<i>Debit</i>	<i>Credit</i>	<i>Dr./Cr.</i>	<i>Balance</i>
Oct.	1		GJ1	1,000		Dr.	1,000
	1		GJ1	4,000		Dr.	5,000
	5		GJ2		300	Dr.	4,700
	5		GJ2		500	Dr.	4,200
	8		GJ2	500		Dr.	4,700
	15		GJ2		100	Dr.	4,600
	20		GJ2	3,000		Dr.	7,600
	30		GJ2		500	Dr.	7,100

Computer Equipment (Hardware)						Account No. 155	
<i>Date</i> 20**		<i>Explanation</i>	<i>PR</i>	<i>Debit</i>	<i>Credit</i>	<i>Dr./Cr.</i>	<i>Balance</i>
Oct.	1		GJ1	900		Dr.	900

Office Furniture and Equipment						Account No. 158	
<i>Date</i> 20**		<i>Explanation</i>	<i>PR</i>	<i>Debit</i>	<i>Credit</i>	<i>Dr./Cr.</i>	<i>Balance</i>
Oct.	1		GJ1	150		Dr.	150
	5		GJ2	2,000		Dr.	2,150
	15		GJ2	100		Dr.	2,250

Accounts Payable/General Liabilities						Account No. 200	
<i>Date</i> 20**		<i>Explanation</i>	<i>PR</i>	<i>Debit</i>	<i>Credit</i>	<i>Dr./Cr.</i>	<i>Balance</i>
Oct.	10	Legal Supplies Inc. ¹	GJ2		580	Cr.	580

Personal Loan						Account No. 205	
<i>Date</i> 20**		<i>Explanation</i>	<i>PR</i>	<i>Debit</i>	<i>Credit</i>	<i>Dr./Cr.</i>	<i>Balance</i>
Oct.	1	James Case	GJ1		4,000	Cr.	4,000

¹ Although an explanation is not required, it may be added if the bookkeeper wishes to provide extra details regarding an entry.

Credit Card Debt						Account No. 210	
Date 20**	Explanation		PR	Debit	Credit	Dr./Cr.	Balance
Oct. 5			GJ2		1,500	Cr.	1,500

Justin Case, Capital						Account No. 300	
Date 20**	Explanation		PR	Debit	Credit	Dr./Cr.	Balance
Oct. 1			GJ1		1,000	Cr.	1,000
	1		GJ1		900	Cr.	1,900
	1		GJ1		150	Cr.	2,050
	8		GJ2		500	Cr.	2,550

Fees Earned						Account No. 400	
Date 20**	Explanation		PR	Debit	Credit	Dr./Cr.	Balance
Oct. 20			GJ2		3,000	Cr.	3,000

Office Supplies/General Expense						Account No. 535	
Date 20**	Explanation		PR	Debit	Credit	Dr./Cr.	Balance
Oct. 10			GJ2	580		Dr.	580

Rent Expense						Account No. 538	
Date 20**	Explanation		PR	Debit	Credit	Dr./Cr.	Balance
Oct. 30			GJ2	500		Dr.	500

Telephone Expense						Account No. 565	
Date 20**	Explanation		PR	Debit	Credit	Dr./Cr.	Balance
Oct. 5			GJ2	300		Dr.	300

FIGURE 4.5 General ledger accounts after October posting completed

Preparing the Trial Balance

A **trial balance** lists all the accounts in the general ledger with the debit or credit balance shown for each account (Figure 4.6). The trial balance is not a financial report, but the information in it is used to prepare financial reports. List the accounts in the trial balance in the same order as they appear in the general ledger. The balance from each of the ledger accounts

must be entered in the appropriate debit or credit column. At the end, the total is calculated for each column, and the total debits must equal the total credits. Draw a single line above the totals and a double line below the totals.

The heading of the trial balance contains three lines. The first line identifies the firm, the second line describes the statement, and the third line shows the date of the statement.

The trial balance is important because it proves that the entries were properly recorded in the general journal, that they were properly posted to the general ledger, and that the balances in the general ledger were correctly calculated.

Justin Case, Paralegal Trial Balance October 31, 20**			
#	Account	Debit	Credit
100	General Bank Account	\$7,100	
155	Computer Equipment (Hardware)	900	
158	Office Furniture and Equipment	2,250	
200	Accounts Payable/General Liabilities		\$580
205	Personal Loan		4,000
210	Credit Card Debt		1,500
300	Justin Case, Capital		2,550
400	Fees Earned		3,000
535	Office Supplies/General Expense	580	
538	Rent Expense	500	
565	Telephone Expense	<u>300</u>	
		<u>\$11,630</u>	<u>\$11,630</u>

FIGURE 4.6 Trial balance

If the totals in the trial balance are not equal, it is likely that one or more errors were made. These must be found before proceeding further.

Finding Errors in the Trial Balance

To find any errors, follow these steps:

1. *Wrong column:* Check to see if a debit amount was entered into the credit column in the ledger account while posting from the general journal.
2. *Wrong column:* Check to see if a credit amount was entered into the debit column in the ledger account while posting from the general journal.
3. *Calculation error:* Check the arithmetic to ensure that an error was not made in calculating one or more balances in the ledger accounts.
4. *Copying error:* Check to ensure that the amounts in the general ledger were copied correctly to the trial balance.
5. *Calculation error:* Check the calculation of the totals in the trial balance.

Some errors will not be revealed even if the debit and credit totals in the trial balance are equal:

- Amounts posted to the wrong ledger account but otherwise correctly debited or credited
- Leaving out an entire transaction when posting from the general journal to the general ledgers
- Compensating errors (an error on the debit side that offsets an error of equal value on the credit side)

Common Mistakes

Trying to find mistakes in the trial balance can be frustrating, so here are a few tricks:

1. There is probably a *mathematical error* if the difference between the total debits and credits is off by 10, 100, 1,000, and so on.
2. There is probably an *omission error* if the difference is equal to the balance in one of the general ledger accounts. The amount may accidentally have been omitted. It is also possible that the number was not posted from the general journal.
3. There is probably a *posting error* if you can divide the difference in debits and credits by two. Check to see if a debit was entered on the credit side by mistake, or vice versa, in the ledger or in the trial balance. For example, a difference of \$60 divided by two is \$30. This means you may have entered a \$30 debit to an account instead of correctly entering the amount as a credit, or vice versa.
4. There is probably a *transposition error* if the difference is divisible by nine. A **transposition** is the accidental reversal of digits—for example, entering \$91 instead of \$19 or \$5,520 instead of \$5,250. When you subtract the numbers from each other and divide the difference by nine, you will get an even number. For example, \$5,520 – \$5,250 is \$270. When you divide \$270 by nine, you get an even \$30. This result indicates a possible transposition error.
5. There is possibly a *slide error*. A **slide** is an error resulting from incorrect placement of the decimal point in writing numbers. For example, \$5,250 may have been entered as \$52.50.
6. There may be a *copying error*. Compare the balances in the trial balance with the ledger accounts to check for copying errors.
7. There may be a *calculation error*. Recalculate the balances in each ledger account.
8. There may be a *posting error*. Trace all postings from the journal to the ledger.

If you cannot find the error after having completed all these steps, take a break. Next time you look at the numbers, the error will probably jump out at you.

Preparing Financial Statements

The trial balance (Figure 4.7) is used to prepare **financial statements**—first the income statement, then the statement of owner's equity, and finally the balance sheet.

The financial statements will not have debit or credit columns. The left column in the income statement (Figure 4.8) and in the statement of owner's equity (Figure 4.9) is used to calculate totals, which are then placed in the column to the right. The balance sheet (Figure 4.10) is displayed with assets on the left-hand side and liabilities and owner's equity on the right-hand side. An additional column can be placed on the right-hand side to add up liabilities if necessary.

The information on the income statement is used to calculate the statement of owner's equity. Once you know the amount of the owner's equity, you are able to transfer that information to the balance sheet, so it is imperative that the statements be completed in the correct order. All the information required for each of the statements is found in the trial balance.

Justin Case, Paralegal Trial Balance October 31, 20**			
#	Account	Debit	Credit
100	General Bank Account	\$7,100	
155	Computer Equipment (Hardware)	900	
158	Office Furniture and Equipment	2,250	
200	Accounts Payable/General Liabilities		\$580
205	Personal Loan		4,000
210	Credit Card Debt		1,500
300	Justin Case, Capital		2,550
301	Justin Case, Drawings		0
400	Fees Earned		3,000
535	Office Supplies/General Expense	580	
538	Rent Expense	500	
565	Telephone Expense	300	
		<u>\$11,630</u>	<u>\$11,630</u>

Balance Sheet Accounts

Owner's Equity Account(s)

Income Statement Accounts

Balance Sheet Accounts

Owner's Equity Account(s)

Income Statement Accounts

FIGURE 4.7 Trial balance showing balance sheet, owner's equity, and income statement accounts

Income Statement

The first statement prepared is the **income statement**, which shows the revenues and expenses for a particular **accounting period** and is sometimes called the profit and loss statement. The heading includes the name of the business, the name of the statement, and the period covered by the report.

The income statement must be prepared at the end of each fiscal year, but is usually prepared more frequently, typically each month, to inform the owner of the bottom line for the period. This information is often required by the firm's bank and investors.

The simple form of the income statement is sufficient for the purposes of a paralegal firm. It will show the revenues earned less the expenses incurred for the period to arrive at a net profit or net loss.

Justin Case, Paralegal Income Statement for the period ended October 31, 20**		
Revenue		
Fees Earned		\$3,000
Expenses		
Office Supplies/General Expense	\$580	
Rent Expense	500	
Telephone Expense	<u>300</u>	
Total Expenses		<u>1,380</u>
Net Income		<u>\$1,620</u>

FIGURE 4.8 Income statement

Reporting Income and Expenses

The Canada Revenue Agency (CRA) website has detailed and extensive information for businesses outlining what is to be declared as income and how expenses can be claimed. The following headings emphasize some (but not necessarily all) of the tax considerations you should be aware of as a licensee when preparing your records for tax purposes. Interpretation Bulletins published by the CRA provide detailed guidelines for interpretation of various sections of the *Income Tax Act* and should be consulted when in doubt.

TAX TIP

Accounting for Your Earnings (Income)

Generally, business income must be reported using the accrual method of accounting. Under the accrual method, you have to report income in the fiscal period you earn it, regardless of when you receive payment. Similarly, you deduct allowable expenses in the fiscal period in which you incur them, whether or not you pay for them in that period. *Incur* usually means you either paid or will have to pay the expense.

Other Income

You must also report the total income you received from other sources, such as a recovery of an amount previously written off as a bad debt in a previous year, and interest income received for late payment of invoices.

Barter Transactions

A **barter transaction** takes place when any two persons agree to an exchange of goods or services and carry out that exchange without using money. If you are involved in a barter transaction, the goods or services you receive could be considered proceeds from a business operation. If you offer legal services to the mechanic who fixes your car, this is considered a barter transaction. You are required to include the value of the goods or services you provided in your income. Barter transactions may also have GST/HST implications.

TAX TIP

Accounting for Your Business Expenses

A business expense is a cost you incur for the sole purpose of earning business income. You must back up business expense claims with a sales invoice, an agreement of purchase and sale, a receipt, or some other voucher that supports the expenditure. If you pay cash for any business expenses, be sure to get receipts or other vouchers. Receipts should include the vendor's name and the date as well as GST/HST information.

As a sole proprietor or partner in a partnership, when recording expenses you should enter only the business part of the expense. This means that the following are not included as part of your expenses:

- Salary or wages (including drawings) paid to self or partner(s)
- Cost of goods or services that you, your family, or your partners and their families used (including such items as food, home maintenance, or business properties)
- Interest and penalties you paid on your income tax
- Life insurance premiums
- The part of any expenses that can be attributed to non-business use of business property
- Most fines and penalties imposed after March 22, 2004, under the law of Canada or a province or a foreign country (this includes parking tickets)

Business-Use-of-Home Expenses

You can deduct expenses for the business use of a work space in your home, as long as you meet *one* of these conditions:

- It is your principal place of business OR
- You use the space only to earn your business income and you use it on a regular and ongoing basis to meet your clients or customers

You can deduct a part of your maintenance costs, such as heating, home insurance, electricity, and cleaning materials. You can also deduct a part of your property taxes, mortgage interest, and capital cost allowance. To calculate the part you can deduct, use a reasonable basis, such as the area of the work space divided by the total area of your home.

Statement of Owner's Equity

The second statement prepared is the **statement of owner's equity**. The heading includes the name of the business, the name of the statement, and the period covered by the report.

The goal of this statement is to calculate owner's equity in the firm after taking into account any profits or losses of the firm less money withdrawn by the owner. The calculation tells us how the owner's investment in the firm has been affected by the operations of the business. You can see that at the end of October, Justin Case's equity in the firm went up to \$4,170 (\$2,550, opening balance + \$1,620, net income) because of the profit from operations during the month of October. The amount of the profit (\$1,620) was added to the capital at the beginning of the period (\$2,550) to calculate the balance in the capital account or owner's equity at the end of the period. If Justin had withdrawn funds from the firm, the amount withdrawn would have been deducted from the net income, resulting in a decrease in the owner's equity.

Justin Case, Paralegal Statement of Owner's Equity for the Period Ended October 31, 20**		
Justin Case, Capital, Oct. 1, 20**		\$2,550
Net Income for Oct. 20**	\$1,620	
Less: Withdrawals for Oct.	<u>0</u>	
Increase in Capital		<u>1,620</u>
Justin Case, Capital Oct. 31, 20**		<u><u>\$4,170</u></u>

FIGURE 4.9 Statement of owner's equity

Balance Sheet

The third statement prepared is the balance sheet. The **balance sheet** is a snapshot of the financial position of the firm on a particular date, typically the end of the financial period being reported. The heading includes the name of the business, the name of the statement, and the date of the report.

The balance sheet provides important information about the financial position of the firm. In Figure 4.10, we can see that Justin has enough cash in the bank to meet his current liabilities. We can also see that his investment in the firm has increased since he started the business on October 1.

Justin Case, Paralegal Balance Sheet October 31, 20**			
Assets		Liabilities	
General Bank Account	\$7,100	Accounts Payable/General Liabilities	\$580
Computer Equipment (Hardware)	900	Personal Loan	4,000
Office Furniture and Equipment	<u>2,250</u>	Credit Card Debt	<u>1,500</u>
		Total Liabilities	<u><u>\$6,080</u></u>
		Owner's Equity	
		Justin Case, Capital	<u>4,170</u>
Total Assets	<u><u>\$10,250</u></u>	Total Liabilities and Owner's Equity	<u><u>\$10,250</u></u>

FIGURE 4.10 Balance sheet

Evaluating the Financial Statements

The financial statements will help provide answers to such questions as:

- Has the firm made or lost money over the period covered by the statements?
- Are the revenues in line with the business plan for the firm or the budget that was prepared?
- Are some of the expenses out of line?
- Does the firm need to cut back, or can it expand?
- Does the firm have sufficient resources to meet its short-term liabilities?
- Does the firm have surplus cash that can be invested to produce income?
- Is the firm at risk of going bankrupt?

CHAPTER SUMMARY

The accounting cycle starts with an analysis of transactions, which are then recorded in a general journal. Once the entries have been added to the journal, they must be summarized; this is accomplished by posting the entries to general ledger accounts and calculating the balance for each general ledger account. The balances in the general ledger are then entered in a trial balance to ensure that the debits are equal to the credits. Once this is ascertained, financial statements—income statement, statement of owner's equity, and balance sheet—can be prepared.

KEY TERMS

accounting cycle, 66	financial statements, 73	post reference (PR), 66
accounting period, 74	general journal, 66	slide, 73
balance sheet, 77	general ledger, 66	statement of owner's equity, 76
barter transaction, 75	income statement, 74	transposition, 73
chart of accounts, 66	opening balance, 66	trial balance, 71

FURTHER READING

Canada Revenue Agency (CRA), "Checklist for Small Businesses," online: <<http://www.cra-arc.gc.ca/tx/bsnss/sm/chcklst-eng.html>>.

Canada Revenue Agency (CRA), "Reporting Business Income and Expenses" (video series), online: <<http://www.cra-arc.gc.ca/vdglly/bsnss/srs-rprtngncmxpns-eng.html?vclp=bsnss/srs-rprtngncmxpns1-eng>>. (See especially Segment 2: Record Keeping.)

Law Society of Upper Canada, *The Bookkeeping Guide for Paralegals* (Toronto: LSUC, February 2014), online: <http://www.lsuc.on.ca/uploadedFiles/PDC/Practice_Review/Paralegal%20Bookkeeping%20Guide%20-%20February%202014.pdf>. (See especially item 7, Clients' General Ledger.)

System for Electronic Document Analysis and Retrieval (SEDAR). The official site that provides access to most public securities documents and information filed by public companies and investment funds with the 13 provincial and territorial securities regulatory authorities (Canadian Securities Administrators), online: <http://www.sedar.com/homepage_en.htm>.

PUT IT INTO PRACTICE

Case Example: Accounting Application

1. When Ann Litigate calculates her company's trial balance, she recognizes that there was an error in the recording of a retainer received from Sam Fisher. The trial balance is understated and out by \$200. How can Ann check and correct this error?
2. On April 5, a new client, Sheila McKay, advised that she would like to retain Ann to commence a small claims proceeding against her neighbour, who borrowed \$10,000 but has failed to pay her back as agreed and as evidenced by a promissory note. Ann prepared the claim for Sheila, and served and filed the plaintiff's claim form at the Small Claims Court (Superior Court of Justice). On June 1, 20***, Ann invoiced Sheila for the services rendered from April 5 to May 30, 20** (invoice #101) as well as for the related disbursements. The total fee charged was equal to \$1,500; the total disbursements (paid by and reimbursable to Ann) were equal to \$200, which included the filing fee, the process server costs, and miscellaneous photocopy/printing costs. Harmonized sales tax (HST; 13 percent) is chargeable on both fees and disbursements. Calculate the total amount of the invoice that would be sent to the client including fees, disbursements, and HST.

REVIEW QUESTIONS

Short Answer

Give a full answer for each question:

1. Identify three kinds of financial statements that are used in financial reporting.
2. What does it mean to “post” to the general ledger?
3. When receiving a payment in cash, does this increase or decrease the general bank account? How do you record an increase in this account? How do you record a decrease?
4. How do you characterize or recognize a payment to the owner of the law firm (e.g., Justin Case) for his services?
5. What is meant by the opening balance on the ledger? What is meant by the closing balance on the ledger?
6. What information gets recorded on the trial balance?
7. How do you find and correct errors on the trial balance?
8. What information gets recorded on the income statement?
9. What information gets recorded on the statement of owner's equity?
10. What information gets recorded on the balance sheet?
11. What is a financial statement, and how do you prepare one?
12. Review, analyze, and discuss one of Air Canada's completed financial statements. To find a statement, go to <http://sedar.com/DisplayProfile.do?lang=EN&issuerType=03&issuerNo=00001324>. Choose “View” to display the company's public records, and then select the most recent audited financial statement from the list (e.g., February 11, 2015).

PRACTICE EXERCISES

Worksheets containing the forms you need to complete the practice exercises are provided separately in the working papers for this chapter.

Practice Exercise 4.1

Using the worksheets provided:

- a. Prepare general journal entries for the following transactions for June Lang that occurred during September 20**.
- b. Post your entries to the general ledgers.

The accounts for June Lang’s firm are the following:

100	General Bank Account	200	Accounts Payable/General Liabilities
120	Accounts Receivable	300	June Lang, Capital
130	Office Supplies	350	June Lang, Drawings
140	Motor Vehicle	400	Fees Earned
158	Office Furniture and Equipment	538	Rent Expense

Transactions:

Sep.	3	June Lang invested \$20,000 cash and office equipment worth \$2,000 in her business
	6	Purchased a motor vehicle on account for \$15,000. She paid \$1,000 by cheque and the balance on credit
	13	Bought office supplies for \$1,000
	15	Withdrew \$500 from the business for personal use
	20	Invoiced Fred Popper \$2,000 for services rendered. Account remains outstanding
	30	Paid rent expense to Minto Developments, \$650

Worksheets:

PRACTICE

EXCEL

June Lang, General Journal					GJ4
Date 20**		Description	PR	Debit	Credit
Sept	3	General Bank Account	100		
		June Lang, Capital	300		

General Ledgers — June Lang

PRACTICE

EXCEL

General Bank Account					Account No. 100	
Date 20**	Explanation	PR	Debit	Credit	Dr./Cr.	Balance
Oct 3	Invest.	GJ4	20,000		Dr	20,000
Oct 13	Motor Vehicle	GJ4		1,000	CR	19,000

Accounts Receivable					Account No. 120	
Date 20**	Explanation	PR	Debit	Credit	Dr./Cr.	Balance

Office Supplies					Account No. 130	
Date 20**	Explanation	PR	Debit	Credit	Dr./Cr.	Balance
Oct 13		GJ4	1,000		Dr	1000

Motor Vehicle					Account No. 140	
Date 20**	Explanation	PR	Debit	Credit	Dr./Cr.	Balance
Oct 6		GJ4	15,000		Dr	

Office Furniture and Equipment					Account No. 158	
Date 20**	Explanation	PR	Debit	Credit	Dr./Cr.	Balance

PRACTICE**EXCEL****Accounts Payable/General Liabilities****Account No. 200**

Date 20**	Explanation	PR	Debit	Credit	Dr./Cr.	Balance

June Lang, Capital**Account No. 300**

Date 20**	Explanation	PR	Debit	Credit	Dr./Cr.	Balance

June Lang, Drawings**Account No. 350**

Date 20**	Explanation	PR	Debit	Credit	Dr./Cr.	Balance

Fees Earned**Account No. 400**

Date 20**	Explanation	PR	Debit	Credit	Dr./Cr.	Balance

Rent Expense**Account No. 538**

Date 20**	Explanation	PR	Debit	Credit	Dr./Cr.	Balance

Practice Exercise 4.2

Using the worksheets provided, post the general journal entries for the following transactions for Frank Piper that occurred during June 20** to the general ledgers.

The partial ledger of Frank Piper uses the following accounts:

100 General Bank Account (Cash)	200 Accounts Payable/General Liabilities
158 Office Furniture and Equipment	300 Frank Piper, Capital

Frank Piper, Paralegal General Journal					GJS
Date 20**		Description	PR	Debit	Credit
		Opening Entries			
June	1	General Bank Account (Cash)		10,000	
		Frank Piper, Capital			10,000
		<i>To record funds invested by owner</i>			
	1	Office Furniture and Equipment		1,000	
		Accounts Payable/General Liabilities			1,000
		<i>Purchased photocopier from Sharp</i>			

PRACTICE**EXCEL****General Ledgers — Frank Piper****General Bank Account (Cash)****Account No. 100**

Date 20**	Explanation	PR	Debit	Credit	Dr./Cr.	Balance
Jun 1	Invest	GJ5				

Office Furniture and Equipment**Account No. 158**

Date 20**	Explanation	PR	Debit	Credit	Dr./Cr.	Balance

Accounts Payable/General Liabilities**Account No. 200**

Date 20**	Explanation	PR	Debit	Credit	Dr./Cr.	Balance

Frank Piper, Capital**Account No. 300**

Date 20**	Explanation	PR	Debit	Credit	Dr./Cr.	Balance

Practice Exercise 4.3

- a. i. Calculate the running balance for the following general ledger account. Indicate whether the balance column has a debit or credit balance.
- ii. Was the account overdrawn at any point?
- iii. What does the post reference refer to?

General Bank Account					Account No. 100	
Date 20**		Explanation	PR	Debit	Credit	Balance
Oct.	1		GJ1	1,000		
	1		GJ1	700		
	5		GJ2		2,000	
	5		GJ2	100		
	6		GJ2	400		
	8		GJ2		100	

PRACTICE**EXCEL**

- b. Calculate the running balance for the following general ledger account. Indicate whether the balance column has a debit or credit balance.

Rent Expense					Account No. 538	
Date 20**		Explanation	PR	Debit	Credit	Balance
Oct.	1		GJ2	1,000		
Nov.	1		GJ2	1,000		
	5		GJ2		30	
Dec.	1		GJ2	900		

- c. Calculate the running balance for the following general ledger account. Indicate whether the balance column has a debit or credit balance.

Accounts Payable/General Liabilities					Account No. 200	
Date 20**		Explanation	PR	Debit	Credit	Balance
Oct.	1		GJ2		5,000	
Nov.	1		GJ2	300		
	5		GJ2		200	
Dec.	1		GJ2	1,000		
	15		GJ2	800		

Practice Exercise 4.4

Comprehensive Problem

The following are transactions for Ann Litigate Paralegal Services that occurred in the month of May:

#	Date 20**	Transaction	Amount
1	May 1	Ann received a cheque from her client, Alan Smith, for legal services provided in a criminal law matter	4,000
2	May 1	Ann took a <u>draw</u> against the firm's <u>equity</u> for her personal use	1,500
3	May 1	Ann paid one month's office rent	1,200
4	May 5	Ann paid for filing fees to the Landlord and Tenant Board on behalf of her client, Ellen Page, with her business credit card	145
5	May 10	Ann paid her telephone and Internet bill	120
6	May 11	Ann purchased accounting software to help manage her bookkeeping	600
7	May 15	Ann paid salary to her assistant	1,000
8	May 15	Ann paid interest expense on her bank line of credit account	90
9	May 18	Ann paid for office supplies on account to replenish her office supplies	250
10	May 25	Ann purchased new office furniture (filing cabinet)	600
11	May 30	Ann paid bank fees and charges for the month of May	30
12	May 30	Ann paid her credit card bill	100
13	May 30	Ann paid for one month of dues to the Law Society	267

Using the chart of accounts found on the inside front cover of this textbook and the worksheets provided:

- Prepare general journal entries for the transactions.
- Post (transfer) the general journal entries to the general ledger accounts.
- Prepare a trial balance.
- Prepare the income statement.
- Prepare the statement of owner's equity.
- Prepare the balance sheet.

The following balances have already been recorded for you in the general ledger for the end of April as the opening balance on May 1:

Ann Litigate, Paralegal Trial Balance April 30, 20**			
#	Account	Debit	Credit
100	General Bank Account	\$3,000	
120	Accounts Receivable	635	
130	Office Supplies	800	
158	Office Furniture and Equipment	5,000	
160	Intangible Assets (Computer Software)	1,865	
200	Accounts Payable/General Liabilities		\$800
210	Credit Card Debt		1,500
250	Bank Line of Credit		5,000
300	Ann Litigate, Capital		5,500
350	Ann Litigate, Drawings	<u>1,500</u>	<u> </u>
		<u>\$12,800</u>	<u>\$12,800</u>

Worksheet a:

[illegible]

PRACTICE

EXCEL

Worksheet b:

PRACTICE**EXCEL****General Ledgers — Ann Litigate**

General Bank Account						Account No. 100	
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	1	Opening balance	✓	3,000		Dr.	3,000

Accounts Receivable						Account No. 120	
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	1	Opening balance	✓	635		Dr.	635

Office Supplies						Account No. 130	
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	1	Opening balance	✓	800		Dr.	800

Office Furniture and Equipment						Account No. 158	
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	1	Opening balance	✓	5,000		Dr.	5,000

Intangible Assets (Computer Software)						Account No. 160	
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	1	Opening balance	✓	1,865		Dr.	1,865

Accounts Payable/General Liabilities						Account No. 200	
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	1	Opening balance	✓		800	Cr.	800

PRACTICE**EXCEL**

Credit Card Debt					Account No. 210		
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	1	Opening balance	✓		1,500	Cr.	1,500

Bank Line of Credit					Account No. 250		
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	1	Opening balance	✓		5,000	Cr.	5,000

Ann Litigate, Capital					Account No. 300		
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	1	Opening balance	✓		5,500	Cr.	5,500

Ann Litigate, Drawings					Account No. 350		
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	1	Opening balance	GJ4	1,500		Dr.	1,500

Fees Earned					Account No. 400		
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	1		GJ4		4,000	Cr.	4,000

Bank Charges and Credit Card Expense					Account No. 507		
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	25		GJ4	30		Dr.	30

PRACTICE**EXCEL**

Salaries Expense						Account No. 511	
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	15		GJ4	1,000		Dr.	1,000

General Disbursement Expense						Account No. 525	
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	5		GJ4	145		Dr.	145

Interest Expense						Account No. 529	
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	15		GJ4	90		Dr.	90

Membership/Professional Dues						Account No. 534	
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	30		GJ4	267		Dr.	267

Rent Expense						Account No. 538	
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	1		GJ4	1,200		Dr.	1,200

Telephone Expense						Account No. 565	
Date 20**		Explanation	PR	Debit	Credit	Dr./Cr.	Balance
May	10		GJ4	120		Dr.	120

Worksheet c:

PRACTICE	
	EXCEL

Ann Litigate, Paralegal			
Trial Balance			
May 31, 20**			
#	Account	Debit	Credit
	Total	=====	=====

Worksheet d:

Ann Litigate, Paralegal Income Statement for the period ended May 30, 20**		
Revenue		
Expenses		
Net Profit	=====	=====

Worksheet e:

Ann Litigate, Paralegal Statement of Owner's Equity for the period ended May 30, 20**		
	=====	=====

Worksheet f:

Ann Litigate, Paralegal Balance Sheet May 30, 20**			
Assets		Liabilities	
		Owner's Equity	
Total Assets	=====	Total Liabilities and Owner's Equity	=====

APPENDIX 4.1

Formats for Financial Statements

The heading consists of three lines.	Name of the Firm Income Statement for the Period Ended _____			
List all sources of income in first column.	Income			
	Source 1	\$ xxx		Use \$ sign on first row.
	Source 2	<u>xxx</u>	\$ xxx	Place total income in second column. Use \$ sign in front of total.
List all expenses from operations in first column.	Expenses			
	Expense 1	xxx		
	Expense 2	<u>xxx</u>		
	Total Expenses		<u>xxx</u>	Place total expenses in second column.
	Net Income		<u>\$ xxx</u>	Calculate income minus expenses to determine profit or loss. Use \$ sign in front of net income or net loss.

FIGURE 4.11 Format for income statement

Heading: Name of firm, name of statement, and period covered by the statement	Name of the Firm Statement of Owner's Equity for the Period Ended _____			Use \$ sign at top of each column and for the total at the end.
Capital at the beginning of the period as shown on worksheet.	Justin Case, Capital, December 1, 20**		\$ xxx	Income for the period from the income statement.
	Net Income for December	\$ xxx		Withdrawals from the worksheet.
	Less: Withdrawals for December	<u>xxx</u>		
Calculate amount of increase or decrease in capital.	Increase in Capital		<u>xxx</u>	Calculate change in capital as at the end of the period. Double underline for total.
	Justin Case, Capital, December 31, 20**		<u>\$ xxx</u>	

FIGURE 4.12 Format for statement of owner's equity

Justin Case, Paralegal Balance Sheet December 31, 20**				← Heading uses three lines.
				← Preparation date.
Assets				
Current Assets				
General Bank Account		\$4,906.91		← Use a \$ sign for the first number in each column.
Trust Bank Account		15,280.00		
Accounts Receivable		25,000.00		
Prepaid Insurance		550.00		
Office Supplies		200.00		
Total Current Assets			\$45,936.91	
Fixed Assets				
Computer Equipment (Hardware)	\$6,520.00			
Less: Accumulated Depreciation on Computer Equipment	<u>326.01</u>	6,193.99		← Carry over calculation from column two.
Office Furniture and Equipment		<u>2,250.00</u>		
Total Fixed Assets			<u>8,443.99</u>	
Total Assets			<u>\$54,380.90</u>	← Add total assets together. Use \$ sign for total. Single line above and double line below total.
Liabilities and Owner's Equity				
Liabilities				
Accounts Payable/General Liabilities		6,890.00		
Personal Loan		3,100.00		
Credit Card Debt		2,500.00		
Accrued Salaries payable		240.00		
Trust Funds Owed		<u>15,280.00</u>		
Total Liabilities			28,010.00	
Owner's Equity				
Justin Case, Capital			<u>26,370.90</u>	
Total Liabilities and Owner's Equity			<u>\$54,380.90</u>	← Total liabilities and owner's equity equals total assets. Single line above and double line below total.

↑
 Column used for calculations only.

↑
 List amounts to be added together in third column.

↑
 Column used for total amount from column three.

FIGURE 4.13 Format for balance sheet